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SUBJECT: POLAND ENERGY SECURITY UPDATE

REF: SEPTEL

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Classified By: DEPUTY ECONOMIC COUNSELOR L. GRIESMER, REASONS 1.4 B, D

11. (C) Summary: Poland's concern about its energy security heightened with the Russian shut-offs of gas to Ukraine, oil to Belarus, and oil to the Mazeikiu refinery through the Druzba pipeline in the last few years. The previous PiS-led government developed a plan and began to take steps to improve Poland's energy security situation. This cable updates GOP efforts at constructing a gas pipeline from Norway to Poland, constructing an LNG port, reversing the Odessa-Brody oil pipeline in Ukraine and extending it to Plock and Gdansk in Poland, cooperation on construction of a replacement for the Ignalina nuclear power plant in Lithuania, and construction of oil storage facilities. Septel will include recommendations on how the USG can work with the GOP to help improve its energy security situation. End Summary.

The Statistics

12. (U) In 2007, Poland's domestic production covered 30% of its approximately 13.5 BCM gas requirements, and Poland imported the other 70%. Of gas imports, 67% were from Russia, 24.5% from Central Asia and 8.5% from Germany. Poland receives most of its gas through the Yamal gas transit pipeline from Russia, which has a 32 bcm capacity. Poland's internal gas pipeline network has a 14.6 BCM capacity.

13. (U) By comparison, in 2007 Poland produced only 4% of its approximate 23.3 million tons of oil requirements domestically, importing the other 96%. 97.5% of oil imports were from Russia, with the remaining 2.5% from Kazakhstan, Norway, and the United Kingdom. Poland's state-owned oil company PKN Orlen's Plock refinery has a 13.8 million ton capacity, which achieved 98.9% usage in 2007. Orlen also

owns a percentage of Czech-based Unipetrol and a share in the Kralupy refinery there, as well as the Mazeikiu refinery in Lithuania. State-owned Lotos Group's Gdansk refinery has a 6 million ton capacity. Lotos also owns two smaller refineries - Czechowice with a 250,000 ton capacity, and Jaslo with 500,000 ton capacity.

¶4. (U) Poland's electricity sector is self-sufficient and largely dependent on its enormous coal reserves. In 2007, 60.35% of electricity production was from bituminous coal, and 33.88% by lignite. Only 2.52% was produced by gas plants, 1.1% by co-generation, 1.75% by hydro, 0.05% by wind, and 0.35% by independent power plants. Poland exported 8,467,466 MWh of electricity in 2007, while importing 3,121,016 MWh.

#### The Previous Government's Plans

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¶5. (U) After the Russian oil shut-off to Ukraine in 2006, Poland's PiS-led government established a national energy security strategy to reduce its dependence on Russia. The government decided to implement the following projects:

- Development of a gas pipeline from Norway to Poland
- Construction of an LNG port in Poland
- Reversal of the Odessa-Brody oil pipeline in Ukraine and extension of the pipeline to Plock and Gdansk
- Strong opposition in international fora to the Nord Stream gas pipeline from Russia to Germany

¶6. (C) The GOP requested, and the USG agreed, to include energy security discussions in the U.S.-Poland Security Dialogue. At USG urging, the GOP pursued membership in the

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International Energy Agency (IEA), which it formally joined in 2007. The GOP also began to actively pursue membership in the group of countries and companies building a replacement for the Ignalina nuclear power plant in Lithuania, as well as construction of an electric power bridge that would connect the Polish and Lithuanian energy grids. State-owned companies began to study options for oil storage in salt caverns on the Baltic coast, recognizing a severe lack of oil storage capacity that precluded Poland's ability to meet IEA and EU storage requirements.

#### The New Government Studies and Waffles

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¶7. (C) The Tusk government elected in late 2007 announced that it would quickly review all energy security projects designed by the previous government and asked state-owned companies to put strategic decisions on hold until the review was completed. As of June 23, 2008, there has been no public announcement of which projects will be allowed to go forward.

Despite the GOP's request to delay decisions on the projects, the companies have continued to pursue work that does not require GOP approval, or have gone ahead anyway arguing that they are not making decisions that are against the government's interests. As opposed to the previous government, in which Deputy Minister of Economy Naimski was considered the "Energy Czar" and was the go-to person on energy issues, no such individual has emerged in the Tusk government. Indeed, many company executives have complained that they have no point of contact in the government on energy issues. The President of PKN Orlen, Poland's largest company, has yet to meet Deputy Prime Minister and Minister of Economy Pawlak.

#### The Gas Pipeline from Norway

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¶8. (C) The proposed 3 BCM gas pipeline from Norway is still on track, but is waiting for decisions by other countries to be realized. This project requires a Norwegian government

decision to build an internal gas pipeline from the Atlantic coast to internal population centers, a gas pipeline from Norway to Sweden or Denmark, internal pipelines in Denmark, then a gas pipeline from Denmark to Poland. Contacts at the Norwegian embassy confirmed that the Norwegian government has not made a final announcement of their decision to move gas from the Atlantic Coast to population centers, but that it is widely expected shortly. The Swedish government must then decide if and where a pipeline from Norway would transit Sweden. The investment decision by the Skanled consortium is expected in the fourth quarter of 2008 or first quarter of 2009. Most of our contacts believe that this project will go forward, although any gas eventually delivered to Poland will be much more costly than Russian gas.

#### LNG Port in Swinoujscie

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19. (C) The GOP tasked state-owned gas company PGNiG with constructing an LNG port. PGNiG and the GOP chose Swinoujscie, on the Baltic Sea in western Poland, as the port's site to avoid concentrating too many energy facilities in Gdansk, already home to Naftoport. PGNiG reports that the detailed technical design of the project has begun and the company expects construction to begin in the fourth quarter of this year. Company contacts believe it will be no problem to obtain external financing for the project, arguing that the financial assumptions used to justify the project are quite conservative. They note that they can request EU funds for construction as the port is on an EU list of infrastructure projects. The major obstacle to the project is obtaining a long-term gas contract. Our contacts report

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that a long-term contract was waiting GOP approval last October, but delayed by the change in government. They expect the contract to be signed in the next two months.

#### Odessa-Brody-Plock-Gdansk

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10. (C) Reversal of the Odessa-Brody oil pipeline in Ukraine and extension of the line to the Plock refinery in Poland and the Gdansk Naftoport have been pursued by a number of Polish governments for political and energy security reasons. President Kaczynski supports the project and has been instrumental in organizing energy summits with his counterparts in Ukraine, Georgia, and Azerbaijan in support of the project. The state-owned oil companies of those countries, as well as Kazakhstan, formed a consortium, New Sarmatia, to pursue the project. New Sarmatia commissioned another feasibility study, by Halliburton subsidiary Grenherne, which completed a 2001 study. New Sarmatia executives expect the results of the feasibility study in October, in time for the next Presidential Summit on energy issues, scheduled for Baku in November. Contacts tell us that the new study will examine the oil market, including refineries in the Baltic region and further afield that can use the sweeter Azeri crude, and will be more professional than the EU-sponsored study completed over a year ago. Most observers believe that this study is the last opportunity for the project to move ahead, although few energy industry insiders give it any serious odds of completion.

#### Nuclear Power Plant and Electric Bridge

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11. (C) Although not on the PiS government's original list of energy security projects, Polish participation in the replacement for the Ignalina nuclear power plant and construction of an energy bridge between Poland and Lithuania became a priority of President Kaczynski and is now supported by many in Poland. Polish electric company officials continue to work with their counterparts in the Baltic states to design a consortium that will allow all four states to participate in the project. Sensitive to criticism about

Poland's demand for at least 1200 MW from the plant, officials tell us that they must receive at least that amount of supply in order to justify construction of the electric bridge and associated energy infrastructure in eastern Poland. While some officials have publicly stated that Poland will construct its own nuclear power plant by 2025, there is no action by any government or utility company to begin such a project. Surprisingly, despite Poland's proximity to Ukraine and the Chernobyl disaster, the level of opposition to nuclear power in Poland is relatively low, although that may reflect the fact that to date, there is no nuclear power plant or project in the country.

#### Oil Storage

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¶12. (C) Poland's lack of oil storage facilities came to GOP official's attention as it prepared to join the IEA. The PiS government ordered state-owned OLPP (a pipeline logistics company) to design and build storage in salt caverns along the Baltic. OLPP and other government officials went to the U.S. to learn about the U.S. Strategic Reserve and the technology capability of the Idaho National Laboratory, as well as studying similar facilities in France. A change in management at OLPP stalled the company's progress on the project. However, both PKN Orlen and Lotos are studying oil storage projects as neither has sufficient storage capacity to meet GOP requirements.

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